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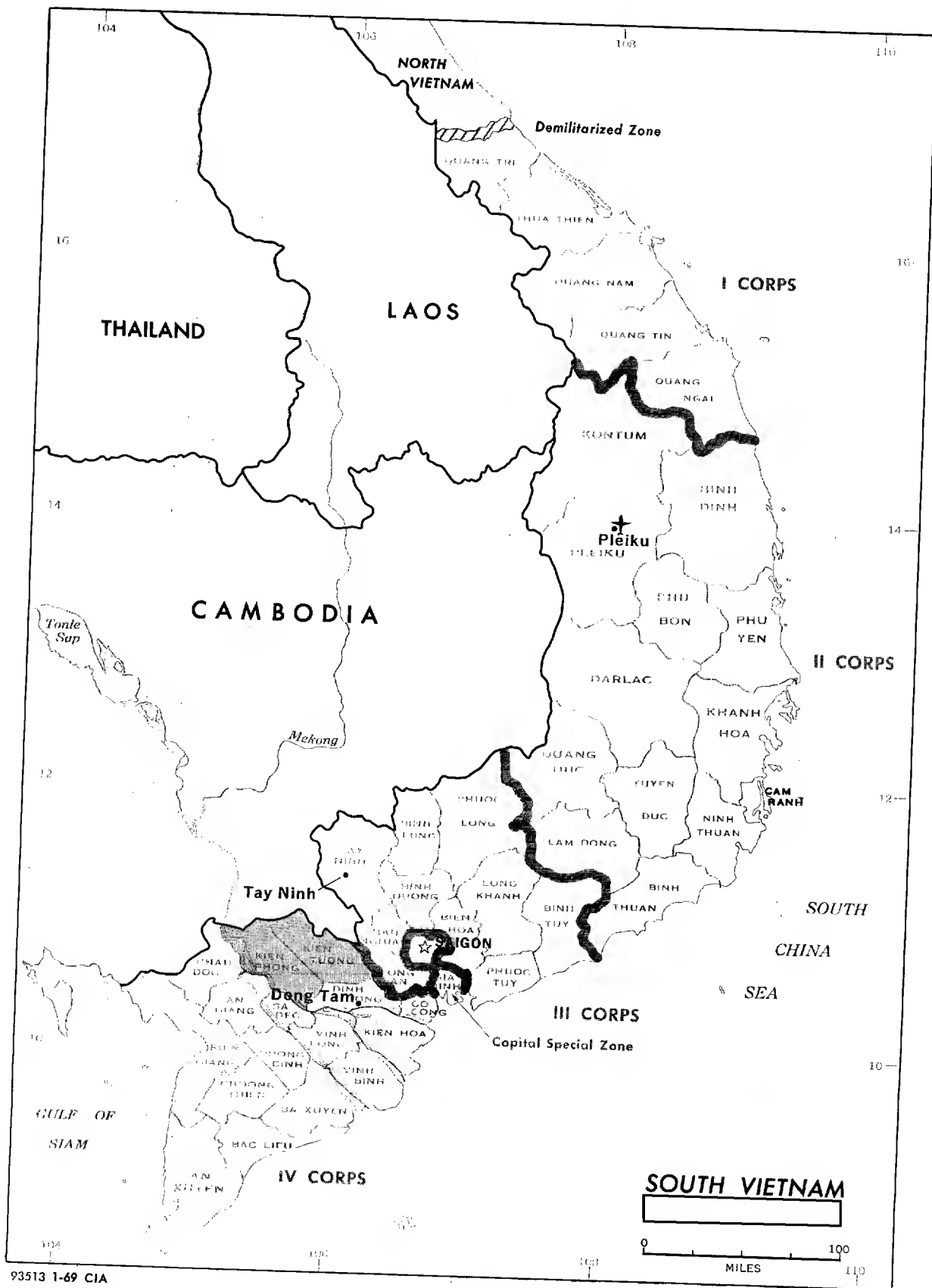
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South Vietnam: Military action picked up sharply in South Vietnam on 14-15 January.

Heavy Communist casualties were reported in two clashes resulting from allied spoiling operations in the delta provinces of Kien Phong and Kien Tuong along known routes of infiltration from Cambodia. Allied losses in these engagements were light; the Communists lost some 139 killed.

Another 122 enemy troops were killed in an attempt to ambush a US convoy near Tay Ninh city. US losses in the seven-hour battle were seven killed and ten wounded, along with one armored personnel carrier destroyed and two trucks damaged.

Communist mortar and rocket crews scored some success on 14-15 January with two attacks on widely separated allied bases. The US 9th Infantry Division base at Dong Tam in the northern delta sustained its third shelling in less than a week. Some 20 120-mm. mortar rounds struck the installation, resulting in US losses of three killed, 28 wounded, and 15 vehicles damaged or destroyed. In the western highlands, Pleiku Air Base was hit by ten rounds of rocket fire, which caused the loss of more than 100,000 gallons of aviation fuel.

(Map)

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Israel - Arab States: [REDACTED]

[REDACTED] no evidence of an Israeli buildup for a major military strike.

[REDACTED] no indicators of a buildup or mobilization. There have been some recent training maneuvers on the West Bank, and Israeli military spokesmen said there had been a routine partial callup of reserves for training. The US attaché suggests that this selective callup may itself have been a reaction to the high state of the Arab alert. On 13 January, an advanced stage of defensive readiness was evident at one of Israel's principal military airfields.

Prime Minister Eshkol made it clear in a speech in the Knesset on 14 January that Israel will continue to defend itself against Arab terrorist attacks. He warned Lebanon and other Arab states again that they would not be "immune" if they allowed terrorists to operate from their soil against Israel.

The Arab states remain extremely uneasy over Israeli military intentions, and Cairo continues to give prominent coverage in its press and radio to reports of an imminent Israeli attack. Lebanese leaders are particularly nervous. Former president Shihab recently told US officials that the terrorist issue bedeviled efforts to form a cabinet, and he again expressed fears that the issue would result in Muslim-Christian conflict.

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UK: An unexpectedly high trade deficit for December has brought increased pressure against the pound and contributed to a rise in gold prices to record levels in London.

Although the December returns do not by themselves suggest any adverse trend, they underscore the increasing urgency of a substantial improvement in the UK's trade performance to reduce speculative pressures on sterling.

After allowing for seasonal influences, the UK's merchandise trade deficit amounted to \$132 million in December, compared with the remarkably small deficit of \$38 million in November.

The key factor in last month's returns was a decline in exports, which has been ascribed to temporary factors such as an extended holiday period and fall offs in exports of ships, aircraft, and diamonds. Merchandise imports, however, increased only very slightly despite above average deliveries of ships ordered by the British.

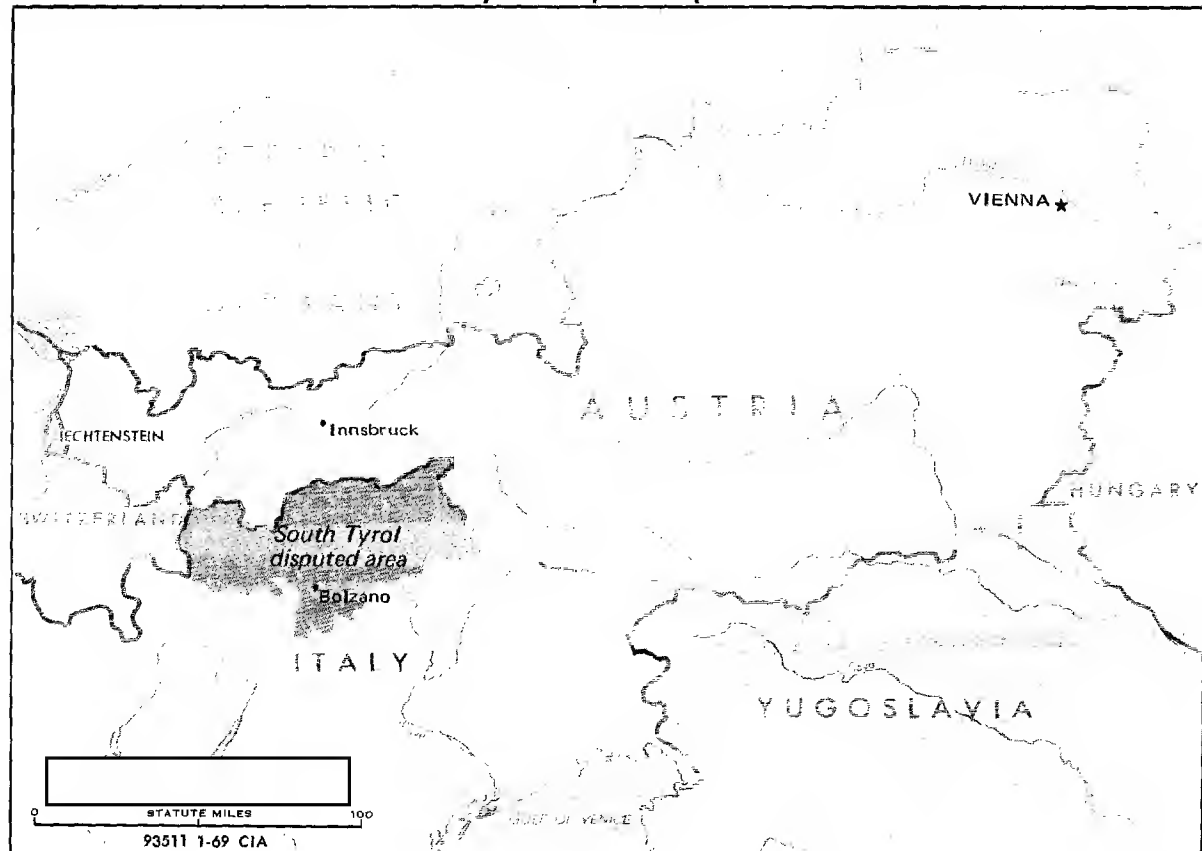
Measured in dollar terms, the over-all 1968 deficit in merchandise trade of about \$1.7 billion represents a slight improvement over the results for 1967. A further improvement in the British trade picture is likely during the first half of 1969 as the import-deposit requirement takes effect.

Much less certain is the prospect for the second half of the year, however, when the regulations governing import-deposits and the agreements for wage restraint expire. In particular, improvements in trade will become increasingly difficult if the government's wage policy erodes further and London thus continues to lose the competitive edge derived from devaluation.

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Austrians See Settlement with Italy over Tyrol Dispute



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Austria-Italy: The Austrians are optimistic that a settlement may soon be reached with Italy over the long-disputed South Tyrol.

Technical experts of both countries have hammered out an agreement providing guarantees for the German-speaking population of this northern Italian area. Austria's foreign minister has said that he believes another meeting of experts later this month will complete work on the agreement and on a timetable for carrying it out.

Chances for amicable settlement in the past have been reduced by the nationalist sentiments of many South Tyrolese and by terrorist activity--

[redacted]
against Italian civil and military installations in the region. The Austrian Socialists have been reluctant to approve any agreement that does not have the full support of the Tyrolese.

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Vienna's current optimism stems from an atmosphere improved by its efforts to reduce terrorism and from a recent agreement among South Tyrolese leaders that the proposed settlement should be supported. Vienna also has decided not to press for international "anchoring" of the agreement, which the Austrian Socialists have been advocating, but to accept, instead, the Italian position that a bilateral agreement is sufficient.

Italy's Foreign Minister Nenni has publicly recommended an agreement, and no doubt believes a settlement would give his ministry an auspicious start. Vienna hopes that Nenni's status as a Socialist leader will further undercut any opposition to the agreement by the Austrian Socialists.

[redacted] (Map)

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Nordic Economic Union: An economic union of Norway, Sweden, Denmark, and Finland has been proposed in a report released in the four countries' capitals.

The union, which would operate within the framework of the European Free Trade Association (EFTA), would seek to harmonize trade and economic policies and establish a customs union and joint administrative institutions. The senior civil servants who drafted the report avoided detailed proposals concerning a common agricultural policy.

The recommendations have met with a varied reaction in the four countries. The Danes, disappointed over their stalemated application for Common Market membership, regard the Nordic proposals as overly modest and favor a tighter union. The Swedes and Finns back the proposed looser cooperation. They estimate that for the short term such an arrangement would be easier to bring about and would forestall individual Nordic countries from making separate arrangements with the European Communities. Norwegian economic interest groups are reluctant to approve the idea of the union, but have decided to go along for the present to test its feasibility.

Although the proposed union would be limited to the economic field, questions have been raised in some Norwegian official circles over the implications for Oslo's foreign and security policies including its NATO obligations.

The prime ministers of the four countries will take up the proposals on 18-19 January, and the interparliamentary Nordic Council will discuss them when it meets in March.

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Colombia: President Lleras has accused labor leaders of attempting a revolution by calling for a general strike next week.

The strike is sponsored by a union front representing many political viewpoints. Top non-Communist labor leaders are cooperating with Communists, in part because of their deepening resentment against Lleras' hard line toward organized labor. They also believe they must protect their positions against Communist efforts to capitalize on public opposition to recent hikes in bus fares and utility rates.

Apparently hoping to avoid a showdown, Lleras has suspended the rate increases in Cali, the southern industrial city where violent protest demonstrations last week led the government to impose martial law. In a speech on 13 January, he was less caustic toward organized labor than in his other recent comments, and he has instructed the labor minister to negotiate settlements to split the strike front. Lleras emphasized, however, that the government will not tolerate continuing public disorder and implied that he holds the Communists responsible.

[Violence broke out again on 14 January in Cali and may recur when students begin classes on 20 January.] Troops have been told to prepare to move quickly into the cities to maintain order if necessary, as was done in Cali.

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Kenya: The current phase of the drive to oust noncitizen businessmen is not expected to have a major adverse impact on the economy, although some distribution problems may arise in the commercial sector.

On 1 January the government notified several hundred Asian shopkeepers that they would not be issued trade licenses this year, but that they would be given up to six months to settle their affairs. The overwhelming number of those affected are British rather than Kenyan citizens, and have been the target of Africanization measures for some time. For the most part they are small rural traders who own stalls that Africans can easily take over and operate successfully.

Africanization measures stimulated the exodus from Kenya of several thousand Asians last year. Little damage to the economy resulted, however, mainly because the government allowed skilled Asians to remain. The government can regulate the pace of Africanization by withdrawing measures if the economy takes a serious downturn or by hardening its line if no adverse effects develop.

[REDACTED]

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India-Iran: The Shah's recent state visit to India was successful from the Indian viewpoint and probably satisfactory to the Iranians.

The 12-day visit, which included talks in New Delhi and a week-long tour of India, topped off a series of high-level Indo-Iranian exchanges over the last year. Since early 1967 the Indians have been cultivating Iran in hopes of reducing the close Iranian-Pakistani relationship, and they gave the Shah the full red carpet treatment. They chose to play down Iran's policy of support for the UN resolutions on Kashmir and Iranian membership in CENTO--both major irritants in their cool relations in the past.

The Shah's strong desire to play the peace-maker in South Asia was gently rebuffed by Mrs. Gandhi, who insists that India's problems with Pakistan must be settled on a strictly bilateral basis. The Indians did, however, risk damaging their highly valued relations with the Arabs by recognizing that "preservation of peace and stability in the Persian Gulf is the exclusive responsibility of the littoral states." The Shah, in turn, acknowledged in the final communiqué that bilateral negotiations are the pre-eminent means for settling issues between states. The Shah's performance throughout the visit and his approach to world and regional problems reportedly impressed the Indians.

On the economic front, it was agreed that "immense" possibilities exist for closer collaboration, especially in the exploitation of petrochemicals. A joint ministerial commission on economic, trade, and technical cooperation is to be created.

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NOTE

Rumania-USSR: Rumanian opposition to the agenda of a summit meeting of the Council for Economic Mutual Assistance (CEMA) has contributed to the postponement of the conference until April,

[redacted] "Pre-liminary" discussions will be held this month, [redacted]

[redacted] Bucharest remains opposed to the supranational and integrative proposals being advanced by Moscow and its other allies. [redacted]

summit meeting of the Warsaw Pact, reportedly also scheduled for this month. [redacted]

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